

FM News

Our new division name...

Public Management, Governance and Participation. (RSGP).

Neil Wallace, who was Director, International Services, ICAS, and previously Developing Nations Technical Manager for IFAC, joined the RSGP FM team as a Senior Financial Management Specialist, on 2 February. Neil's primary function is to provide guidance on how to conduct financial due diligence and to support operational teams in the design and processing of loans and grants.

Financial Management and Analysis Training Course The next 4 day course is scheduled for Manila in May 2009. Please contact us to register or to get course details etc.

Revised and updated Due Diligence Methodology Note is now on FM C³ [Link to FM CoP database \(C³\)](#).

Recently Asked Questions

Q. I am aware that taxes and duties are now allowed as eligible project expenditure – but do this new eligibility cover all taxes and duties such as Income Tax, Import Duty, Value Added Tax etc or are there any exceptions.

A. ADB's policy on allowable expenditure was expanded in March 2006 and items such as bank charges, interest during construction and taxes and duties were added to the list of eligible items. The general position in taxes and duties is that they are eligible, including income tax on salaries of resident tax-paying project staff (e.g. PMU staff). Relevant costs should be included in the project cost estimates and shown separately in the Cost Estimates table in the Report and Recommendation of the President (RRP).

There are exceptions to the general rule because a threshold is set in the Country Partnership Strategy (CPS) which may restrict or limit what can be paid. Initially as part of the development of the CPS a review of the tax regime is undertaken and if any part is found to be excessive, the eligibility status will be amended. For example, a DMC

imposes import duties of 30% which ADB recently judged as unacceptably high and therefore import duties on project plant and machinery were not eligible for re-imbursement. The threshold is documented in an Appendix to the CPS and therefore this should be checked when considering eligibility.

Q. Can retroactive financing be used to cover relevant preliminary project cost incurred during the project development and approval process?

A. Yes. Retroactive financing is permitted provided it is agreed in advance and is identified in the RRP. In essence, retroactive financing refers to financing of project expenditures incurred before the loan agreement or TA agreement becomes effective. Typically, it would cover essential project related works or procurement that needs to be carried out during the development process in order to enable the project to be implemented with minimum delay. Relevant costs must be included in the project costing and thus will have been included in the financial and economic evaluation of the project.

Generally, the expenditure must have been incurred no earlier than 12 months before effectiveness date. In exceptional circumstances, a longer period could be allowed. The allowable amount is limited to 20% of total project cost.

Retroactive financing cannot be used to cover additional costs that emerge during a project because of additional or unforeseen items of expenditure coming to light or because of a higher than forecast costs. This eventuality must be covered by supplementary financing which requires formal approval based on an RRP. Retroactive financing is allowable in the case of program loans but only where policy reforms, which formed a

condition precedent of Board approval to the program loan necessarily began before signing. The RRP should give details and identify that the first drawdown tranche is linked to successful achievement of the specific policy initiative.

Q. What are ADB's requirements in terms of Performance Audits?

A. Performance audits refer to specific examination of a program or function of a governmental or public sector entity. Like financial audits, performance audits are not designed to detect fraud, instead, they are typically focused on the 3 "e"s – i.e. economy, efficiency and effectiveness and are targeted at detecting waste and abuse of resources. Also they should not be confused with special purpose audits, such as a project audit which is a specific ADB requirement for project lending and which is conducted to the same standard as the statutory financial audit.

In recent years there has been increased use of performance audit by Supreme Audit Institutions (SAIs) and there is a growing appreciation of its value in terms of strengthening business operations.

IFAC's standard ISAE 3000 is the accepted standard used by the big audit firms. International Association of Supreme Audit Institutions (INTOSAI) has published principles of performance auditing and some SAIs, particularly in USA and Europe have developed practice guidelines. But a major constraint in the ADB context is that many SAIs in DMCs do not have the capacity to conduct performance audits.

ADB does not require performance audits, although the use of these audits may be considered in certain circumstances. However, performance audits require a high level of technical competence. MDBs tend therefore to focus on assisting DMC SAIs to develop internal capacity to conduct efficient and effective financial audits; performance audits skills can then be developed.

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FM CoPr is open to FM specialists and anyone interested in FM topics.
[Contact Lizzette for details.](#)

